HOUSE FISCAL AGENCY

MEMORANDUM

DATE: March 1, 2010

TO: Interested Parties

FROM: Mitch Bean, Director

RE: Background and Issues Concerning Biennial Budgeting

If the State of Michigan adopts and implements biennial budgeting, a number of issues should be considered. Most of these issues can all be addressed through implementing legislation.

Fiscal Period

According to the National Conference of State Legislatures, 20 states practice some form of biennial budgeting (down from 44 states in 1940 and 27 states in 1968). The degree to which those states practice true biennial budgeting varies, as some states commonly enact annual revisions to the initial biennial budget.

All but three of the 20 states maintain 12-month fiscal years, adopting budgets for two consecutive fiscal years simultaneously. Three states (North Dakota, Oregon, Wyoming) have adopted a 24-month fiscal period.

Under either scenario, Section 2200 of the codification of Governmental Accounting and Reporting Standards (GASB) requires a Comprehensive Annual Financial Report (CAFR). Simultaneously adopting budgets for two consecutive fiscal years would accomplish the goal of biennial budgeting, and facilitate the need to produce a CAFR.

The state's budget would need to be balanced and the books closed for the first fiscal year mid-way through the two-year period, and adjustments would need to be made explicitly to the budget for the second year in response to changes in revenue estimates and/or expenditure pressures. Under this scenario, decisions on needed adjustments to balance the state's budget could not be pushed forward for more than 12 months.

Switching to a 24-month fiscal period would involve substantial costs in reprogramming or replacing the state's accounting system. Note however that, under government accounting standards, a comprehensive financial report would still need to be issued for the state on an annual basis.

Legislative Oversight

Changing to a biennial budget process could result in inadequate information for legislative oversight between the initial enactment of appropriations bills and the end of the two-year fiscal period. Once a budget has been put in place for a two-year period, the governor's administration may have less incentive to share information with the Legislature regarding budget implementation in a timely manner.

One option would be to require the various state departments and the State Budget Office to submit detailed spending plans for each appropriation line item to the relevant House and Senate appropriations subcommittees and fiscal agencies within 15 days of their approval by the State Budget Office.

This would include all spending plans and supporting detail submitted by the departments to the State Budget Office in compliance with section 371 of the Management and Budget Act, MCL 18.1371. Spending plans would offer legislators a measure of oversight over budget details to ensure that spending remained consistent with legislative priorities.

Detailed spending plans would include planned spending by fund source and by program/PCA code for the fiscal period. Information would also include allocations of specific contracts to be funded for each line item by fund source and the total cost of each FTE position to be funded for each line item. Spending plan updates, where applicable, would be submitted to the subcommittees and fiscal agencies on at least a quarterly basis.

Along with this information, the State Budget Office would be required to submit any proposed budget adjustments (supplementals/transfers) needed to implement changes in the spending plans on a quarterly basis. By requiring this information on a regular basis, the possibility of budget adjustments being delayed until the end of the second year of the two-year period—when they could potentially involve very large amounts of money—would be avoided.

Other Issues to Consider

- Changes may need to be made to the mechanisms used to adjust the budget to ensure that the Legislature had an appropriate role in budget decision making. Currently, both legislative transfers and executive order reductions require approval only by the two appropriations committees. Under a biennial budget process, the magnitude of the budget adjustments made through those mechanisms could increase substantially due to the longer time horizon over which revenues and caseload expenditures would need to be forecast.

- The provision in the state's constitution that allows the Legislature to reject increases in rates of compensation for classified state employees (Article XI, section 5) may need to be amended to provide for such consideration of compensation increases to occur on a biennial, rather than annual, basis, in order to be consistent with the new budget process.

- A House member serving three full terms would only vote to adopt a new budget three times before he or she was term limited from office. Additional steps would need to be taken to ensure that legislators were given the opportunity to learn about the state budget. NCSL reports that the Speaker of the House in Arkansas recently stated that legislators in that state did not have adequate opportunity under a biennial budget process to familiarize themselves with the state budget and process. (Arkansas is moving from a biennial process to an annual process starting in 2010.)

- A new process may be need to be developed for considering and adopting necessary changes to the budget for the second year of the two-year period. NCSL notes that, "Connecticut's experience has been that budget revisions and adjustments to account for new programs cause off-year budget revision to be about as time-consuming as creation of the full budget." (Connecticut is the state that switched from annual to biennial budgeting most recently, in 1991.)

***Note:** All information attributed to NCSL is taken from the issue brief, " Annual and Biennial Budgeting: The Experience of State Governments," which is available at* http://www.ncsl.org/Default.aspx?TabID=12658.